

Testimony of Roger Bate, PhD, Resident Fellow American Enterprise Institute,  
on “The G8 Summit and Africa’s Development,” before the Committee on International  
Relations’ Subcommittee on Africa, Global Human Rights and International Operations,  
Thursday, June 30, 2005, at 2:00 p.m., in Room 2172 of the Rayburn House Office  
Building.

Mr Chairman,

Thank you for inviting me to testify on behalf of the American Enterprise Institute.

### **Africa’s Great Leap Forward**

This is Africa’s year. Many powerful people are pushing for debt relief and increased aid for the poorest countries, and notably for the entire African continent. But although it is likely that the approach proposed by the UN and the Africa Commission headed by British Prime Minister and G8 host, Tony Blair, will be a huge boon for the aid industry, it is destined to fail in its goal of lifting millions out of poverty. The failure will not stem from a shortage of good will on the part of policy makers and citizens of wealthy nations, but because the theory on which the proposed massive transfer of aid is based is fundamentally flawed.

That is not to say that specific aid projects, especially humanitarian relief efforts, cannot be effective, even vital, but that systemic aid has not proven successful. And though it is likely that future aid can and will be done better than in the past, the perverse incentives that doom even the best designed aid projects remain. Thus, it is very likely that more large-scale aid will again result in failure.

Nevertheless, the US administration has gone further than other G8 nations to ensure that the incentives faced with aid delivery are as good as possible. By requiring good institutional changes BEFORE aid is provided, the Millennium Challenge Account avoids a common aid pitfall: assuming that aid can promote sustainable policy improvements in countries where domestic stewardship of such changes is absent. However, as the experience of the MCA has demonstrated, such a careful and targeted approach to aid is difficult, slow, and decidedly unglamorous.

Economic growth depends on qualitative, not quantitative factors; the structure of property rights, whether and how the rule of law is applied, how large government is and how effective it is at delivering public services, how open the economy is to local and international trade. Having such information makes it easier to devise and target aid strategy, which should focus on short run, primarily humanitarian efforts, to governments that are already reforming.

### **Poverty Gap Theory**

Development economists, led by the UN’s Jeffrey Sachs, continue to promote the ‘poverty gap’ theory of development, which argues that poverty prevents the accumulation of savings, which results in low investment and hence low growth. Foreign

aid, therefore, fills the apparent gap between insufficient savings and the requisite level of investment in the economy. Even though economists, notably Peter Bauer, compellingly argued that savings were the “result of economic achievement, not its precondition,” aid has continued to flood into poor nations.

Furthermore, Bauer explained how the elite benefited from aid, which is why it has survived while failing so often: foreign aid was “an excellent method for transferring money from poor people in rich countries to rich people in poor countries.”<sup>1</sup>

### **Africa’s Aid receipts**

Inflation adjusted, Africa has received well over \$400 billion in foreign aid since 1960. According to World Bank data, African GDP per capita on average declined 0.6% every year between 1975 and 2000, which massively increased the number of Africans surviving on less than \$1 a day.

Development expert, Dr Marian Tupy of the Cato Institute, explains that ‘in contrast, South Asia (Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka) performed much better. Between 1975 and 2000, South Asian GDP per capita grew at an average annual rate of 2.94 percent. Yet, between 1975 and 2000, the per capita foreign aid that South Asians received was equal to 21 percent of that received by Africa. The link between foreign aid and economic development seems quite tenuous’<sup>2</sup>.

Foreign aid has probably exacerbated corruption and theft of African leaders:<sup>3</sup> These leaders have embezzled these sums.

- General Sani Abacha of Nigeria: \$20 billion
- President Félix Houphouët-Boigny of Ivory Coast: \$6 billion
- General Ibrahim Babangida of Nigeria: \$5 billion
- President Mobutu Sese Seko of Zaire: \$4 billion
- President Mousa Traore of Mali: \$2 billion
- President Henri Bedie of Ivory Coast: \$300 million
- President Denis N'guesso of Congo: \$200 million
- President Omar Bongo of Gabon: \$80 million
- President Paul Biya of Cameroon: \$70 million
- President Haile Mariam of Ethiopia: \$30 million

Due to corruption, aid proponents have begun to make governance a condition of aid. But many still focus on low aid flows, a colonial past and unfair trade relationships. Jeffrey Sachs says “The poor are blamed for their problems. We say the poor are poor because

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<sup>1</sup> Dorn, James. “P. T. Bauer’s Market-Liberal Vision.” *The Freeman: Ideas on Liberty*. October 2000

<sup>2</sup> See Marian Tupy, forthcoming Cato policy analysis, ‘Trade Protectionism and Poverty in Sub-Saharan Africa’.

<sup>3</sup> George B.N. Ayittey, Ph.D. “Corruption, the African Development Bank, and Africa’s Development” (testimony, U.S. Senate Foreign Relations Committee, Washington, DC September 28, 2004).

they are corrupt or because they don't manage themselves. But in the past two years I've seen exactly the opposite.... The idea that African failure is due to African poor governance is one of the great myths of our time.”<sup>4</sup>

But as Marian Tupy shows ‘evidence is not on Professor Sachs’s side.’ African corruption has been getting worse not better over the past few years.<sup>5</sup>

Having said that, the spread of democracy enables more Africans to vote corrupt governments out of office and that is surely a step in the right direction. And as historian Jeffrey Herbst demonstrates, only one African leader, the Prime Minister of Mauritius, was voted out of office between 1960 and 1989. But between 1990 and 2004, 23 African heads of state were voted out of office<sup>6</sup>.

But an increase in democracy does not always end corruption. And a sad if not unique feature of African nations is that many people continue to see participation in the government as a means of becoming wealthy, and weak institutions allow them to succeed.

For example, Zambia’s former leader, Frederick Chiluba was elected in 1991 partly with the notion of defeating corruption but he has been indicted for embezzling tens of millions of dollars. But today, as Tupy puts it, ‘in an absurd twist, President Levy Mwanawasa, Zambia’s current leader, promised to pardon Chiluba if the latter returned 75 percent of what he had stolen’.

Zimbabwe’s President, Robert Mugabe, has overseen a collapse of his country’s economy, with rampant inflation and a life expectancy that has plummeted from 55 years in 1980 to 33 years in 2005<sup>7</sup>. Yet Mugabe and his wife regularly buy millions of dollars worth of goods from Malaysia, and live the life only imagined by former colonial leaders.

### **Does AID improve growth?**

Ignoring anecdotal examples of corruption and aid failure, empirical justification for the ‘poverty trap’ notion were fairly weak until a widely cited 2000 paper in the prestigious *American Economic Review*. The paper by World Bank economists Craig Burnside and David Dollar showed that “aid has a positive impact on growth in developing countries with good fiscal, monetary, and trade policies but has little effect in the presence of poor policies.”<sup>8</sup> These results, based on data from the years 1970-1995, were influential in promoting aid and the current MCA approach. The Economist magazine even stated,

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<sup>4</sup> Eiatar, Daphne. “Spend \$150 Billion Per Year to Cure World Poverty.” *The New York Times*. November 7, 2004

<sup>5</sup> Tupy forthcoming

<sup>6</sup> Herbst, J. “The Incomplete Triumph of Democracy in Africa” *Bradley Lecture Series*. November 1, 2004, American Enterprise Institute, Washington DC.

<sup>7</sup> See Tren and Bate, Despotism and Disease <http://www.fightingmalaria.org/research.php?ID=32>

<sup>8</sup> Burnside, Craig and David Dollar. 2000. “Aid, Policies, and Growth.” *American Economic Review*. 90 (4): 847-68.

‘there is now a strong body of evidence...that aid does boost growth when countries have reasonable economic policies’. Certainly, UN Millennium Commission Director, Jeffrey Sachs, subscribes to this view.

However, William Easterly, a former World Bank economist, found that when Burnside and Dollar’s data sets were brought more up to date (1970-1999), aid’s role in development was less certain. And Easterly, Levine and Roodman (2003) found no statistically significant interaction between aid and policy.<sup>9</sup> In short, even in the most favorable of policy environments, there remains little support for the initial assertion that aid promotes economic growth.

Empirical research does not support the ‘poverty trap’ notion; even the theory of the poverty trap itself is illogical, since it suggests that no one can ever develop out of poverty. Obviously, nations have, and continue, to develop without massive infusions of aid. All western nations have developed by hard work, saving small amounts at first, and good institutions like strong protection of private property and sensible, well defined and limited public sector regulation. Moreover, aid is often spent on projects that benefit political elites rather than citizens, thereby supporting corrupt regimes and often crowding out private sector initiatives.

Aid creates perverse incentives for donor and recipient, incentives that are certainly not amenable to economic growth. As Harvard University historian David Landes in the *Wealth and Poverty of Nations*, writes: ‘History tells us that most cures for poverty come from within. Foreign aid can help, but, like windfall wealth, can also hurt. It can discourage effort and plant a crippling sense of incapacity...at bottom, no empowerment is so effective as self-empowerment’.

### **The G8 Plan – Making Poverty History?**

There is no doubt a tragic premature loss of life in many part of the world. However, the question for policy makers is, “Will more aid help?” Perhaps wealthy countries can, and should, help with well targeted and well measured humanitarian (and other specific) projects, but economic growth depends strongly on the domestic stewardship of good policies and institutions in developing countries.

However, the current push, driven by UK hosts, is not towards this sound development policy. Instead, it is aimed towards the rhetorically pleasing, but until now unrealistic, target of donations and loans to poor countries totaling 0.7% of wealthy country GDP in foreign aid. Aside from the dubious rationale underlying this effort, it is hypocritical of world leaders to sign up to targets and timetables without real thought as to whether they are deliverable or not. In fact, wealthy nations have already promised and, with the exception of a few small Northern European countries, failed to deliver on the 0.7% pledge for the past two decades.

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<sup>9</sup> Easterly, William, Ross Levine and David Roodman. 2003. “New Data, New Doubts: A Comment on Burnside and Dollar’s ‘Aid, Policies, and Growth’ (2000).” National Bureau of Economic Research working paper No. 9846, July 2003.

Major targets, especially those for health, are replete with failure (e.g. WHO targets - 1978 announcement of Health for All by 2000, which obviously has failed, the Roll Back Malaria announcements of 1998, which have been followed by increases in the malaria rate, and the 3 by 5 initiative to treat 3 million AIDS patients with antiretroviral drug therapy by 2005, which is also failing).

Indeed, in a rare moment of cogency, in 2004, WHO Director General Lee warned that “if we cannot reach 3 by 5, there is no reason to believe we will achieve the Millennium Development Goals.” And now that Dr Lee has confirmed that the 3 by 5 target will not be hit, we need only wait for the UN’s unfulfilled MDG’s to be replaced by another quixotic set of targets.<sup>10</sup>

But regardless of past failures, if the G8 rallies the funds, the UN would coordinate massive aid through the various large agencies (World Bank, IMF, WHO etc.) The aid would deliver complex solutions (nitrogen-fixing plants, bed nets, water recycling etc.) to complex problems (nutrient-poor soils, malaria, high water salinity etc.) in areas of extremely low capacity. It is predicted that increasing aid spending by tens of billions of dollars each year until 2025 will spring the poverty trap for good and all.

As shown previously, there is little support for the idea that a poverty trap exists at the international level. Lack of both good governance and rule of law, among other factors, keeps citizens poor and foreign aid that props up regimes which starve their people of these institutions is a sure way to starve them of bread, as well. For instance, many developing countries have tariffs and taxes on essential medicines, a self-inflicted, regressive and economically inefficient impediment to access to medicines that keeps their citizens from achieving decent health.

In the real world it is the alternative approach of tailored aid to specific projects and marginal reform of institutions that is promoted by economists like Bill Easterly, author the *Elusive Quest for Growth*, which has proved most successful, especially among the Asian tigers. Despite beginning a half century ago with the same level of GDP, and receiving much less foreign aid than their African counterparts, the Asian nations have boomed.

The US has made great strides with the more sensible, ‘Bill Easterley’, approach towards aid. In addition to the MCA, support for humanitarian projects will certainly benefit many in poor nations. Initiatives like the recently announced \$647 million in food aid for East Africa, the \$15 billion President’s Emergency Plan for AIDS Relief (PEPFAR), and the over \$1 billion already donated to the Global Fund to fight AIDS, Malaria, and Tuberculosis, will give short term assistance many need. They are important and worthy projects that will save lives and should be carried out with the greatest possible care and efficiency, but they cannot, on their own, lead to economic growth.

Unfortunately, not all of the humanitarian assistance that the US Congress has allocated to developing countries is being administered properly. Though the MCA is an excellent initiative, the United States Agency for International Development is still responsible for

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<sup>10</sup> Allen, K. HIV drug target ‘will not be met’, 29<sup>th</sup> June 2005. *BBC World*.  
<http://news.bbc.co.uk/2/hi/health/4629933.stm>

the vast majority of US foreign aid. As I have documented in a coauthored paper and testified about before both houses of Congress<sup>11</sup>, during the past decade, USAID has largely squandered the over \$400 million Congress allocated the Agency to fight malaria. USAID has consistently failed to account for its malaria spending, usefully measure its programs, and invest in the interventions proven to prevent and treat a disease that kills over a million pregnant women and children in the developing world each year. Most disturbingly, the Agency's startling lack of transparency means that its other programs, which have not been subject to the same level of scrutiny, may be run just as poorly. . And if the expected Presidential announcement today allocates more funding to malaria control, it would be unfortunate if it were to be handled by exactly the same people who have overseen past failures.

Investing scarce resources in terrible diseases like HIV/AIDS and malaria is a good idea, but the US Congress must demand that the agency it entrusts to handle these funds is fully accountable and spending the money properly. Before the MCA begins to operate on a larger scale, Congress would be wise to ensure that the MCA has the proper mechanisms in place to operate transparently and with fully accountability to US taxpayers

Finally, the US has taken encouraging positions on development issues in the run up to the G8 meeting in Scotland. Most notably, it has smartly opposed the proposed UK-driven International Finance Facility. Not only does the IFF violate the US's fiscal laws (as well as the laws of fellow G8 members Canada and Japan) by requiring a long term budget commitment, it is an uncertain and unrealistic scheme to transfer large sums of aid to countries that will likely not use it well. It is exactly the way aid should not be done.

The US has also admirably pushed for a sensible debt relief plan with its recent agreement to write-off \$40 billion of largely unrecoverable debt from 18 poor countries (it has drawn the rest of G8 to an agreement - to be finalized in Scotland). Compromising from its earlier position, the US agreed to help compensate the lenders (i.e. the IMF and World Bank) who will absorb the main cost of such a move. Showing fiscal responsibility, the US has held firm that the debt write-off should not be financed by the sale of IMF gold reserves, nor should new lending to forgiven countries begin atop the write-off. It aims to provide these countries with a balance sheet advantage so they can borrow more easily from the capital markets.

### **Economic Freedom Will Save Lives**

Popular support for assisting those in poor countries is gaining momentum through the encouraging Make Poverty History campaign. The group, creditably, wants to end world poverty, and part of the purpose of the event will be to influence the July G8 summit, which will concentrate on the questions of African poverty and Climate Change.

There is a lot about Make Poverty History's agenda that makes sense. They oppose export subsidies, which distort trade at the expense of the developing world's poor. They also

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<sup>11</sup> Bate, R. and Schwab, B. "The Blind Hydra: USAID Policy Fails to Control Malaria." Working Paper, The American Enterprise Institute. [http://www.aei.org/publications/pubID.22355/pub\\_detail.asp](http://www.aei.org/publications/pubID.22355/pub_detail.asp)

advocate the cancellation of debt. In some cases, this makes sense -- why should former collapsed states that are striving to join the modern world be penalized for the actions of past despots they have overthrown?

Yet Make Poverty History advocates that developing countries adopt protectionist policies even as developed countries open up their markets. This ignores some basic economic facts: that trade promotes economic progress and that the invisible hand of the market directs buyers and sellers towards activities that promote the general good.

Consider that, for decades, India was one of the countries caught in the trap, seeing its living standards fall during the 60s and 70s as the exact strategies recommended by Make Poverty History were implemented there. Since India began to liberalize, its economy is growing at 8%-10% a year and its poor are becoming less so. Make Poverty History's "trade justice" approach is a recipe for more poverty.

## **Conclusion**

The US approach to aid and trade development is broadly correct. As the MCA rolls out the grants to countries (currently Madagascar, Honduras, Nicaragua and Cape Verde), and assuming it isn't rushed into delivery aid thoughtlessly, and continues to measure performance relationships with GDP, we will see, once and for all, whether aid really does lead to development. After 50 years of widespread failure, this is more important than throwing billions at non-implementable projects of often dubious value.

Poverty will not be made history by aging rock stars and good will, but by sound institutions and domestic growth. Aid has a role to play, especially in humanitarian relief, but it is a minor one, and can be counter productive if not done carefully.

Thank you Mr Chairman,

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